



DEPARTMENT OF THE NAVY
OFFICE OF THE SECRETARY
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SECNAVINST 7510.7F
AUDGENAV

DEC 27 2005

SECNAV INSTRUCTION 7510.7F

From: Secretary of the Navy

Subj: DEPARTMENT OF THE NAVY INTERNAL AUDIT

- Ref:
- (a) DoDDIR 7600.2, "Audit Policies" (20 Mar 04) (NOTAL)
 - (b) GAO, "Government Auditing Standards", GAO-03-673G (ed. Jun 03)
 - (c) DoDINST 7600.6, "Audit of Nonappropriated Fund Instrumentalities and Related Activities" (16 Jan 04) (NOTAL)
 - (d) DoD 7600.7-M, "DoD Internal Audit Manual" (Oct 99) (NOTAL)
 - (f) SECNAVINST 5200.35D, "Department of the Navy Management Control Program" (10 Dec 97) (NOTAL)
 - (g) DON Local Audit Manual
 - (h) SECNAVINST 5200.34E, "Management of Audit Decision and Follow-up Functions" (7 Nov 05))
 - (e) SECNAVINST 5430.7N, "Assignment of Responsibilities in the Office of the Secretary of the Navy" (9 Jun 05)
 - (i) DoDDIR 7600.10, "Audits of States, Local Governments, and Non-Profit Organizations" (17 Mar 04)
 - (j) SECNAVINST 5430.92A, "Assignment of Responsibilities to Counteract Fraud, Waste, and Related Improprieties within the Department of the Navy" (20 Aug 87)
 - (k) SECNAVINST 5520.3B, "Criminal and Security Investigations and Related Activities within the Department of the Navy" (4 Jan 93)
 - (l) SECNAVINST 5740.25D, "Relations with the Office of the Assistant Inspector General for Auditing (AIG(A)), Department of Defense (DoD)" (1 Aug 00)
 - (m) SECNAVINST 5211.5D, "Department of the Navy Privacy Act (PA) Program" (17 Jul 92)
 - (n) Inspector General Act of 1978, 5 U.S.C. App 3, as amended
 - (o) National Defense Authorization Act for Fiscal Year 1996, Pub. L. No. 104-106, § 810, 110 Stat. 186 (10 Feb 96)
 - (p) SECNAVINST 5720.42F, "Department of the Navy Freedom of Information Act (FOIA) Program" (6 Jan 99)

- (q) DoD 5200.1-R, "Information Security Program" (Jan 97)
- (r) DON FOIA Program Update/Policy Change
(8 Jan 03) (modifying ¶ 14k, entitled "Naval Audit Service reports")

1. Purpose

a. This instruction informs Department of the Navy (DON) management officials about DON internal audit policies and procedures. It requires all DON internal audits (whether performed by the Naval Audit Service or command or activity audit organizations) to comply with Department of Defense (DoD) guidance and the Government Accountability Office's (GAO's) *Generally Accepted Government Auditing Standards (GAGAS)*, references (a) through (d).

b. This instruction implements reference (e). With issuance of this instruction, all Secretary of the Navy (SECNAV) instructions governing DON internal audits and the DON internal audit function will be consolidated in one instruction.

2. Cancellation. SECNAVINST 7510.7E is cancelled.

3. Scope. This instruction applies throughout the DON to all audits by DON personnel or activities. All such audits will comply with this instruction, with DoD guidance, and with GAGAS, references (a) through (d).

4. Background. The requirement for an internal audit function within DoD originated in the National Security Act Amendments of 1949 (enacting some of the Hoover Commission Report's recommendations). The requirement was expanded to other executive agencies in section 113 of the Budget and Accounting Procedures Act of 1950.

5. Definition. This instruction provides the definition of audits performed by Naval Audit Service, non-appropriated fund organizations, and DON local audit organizations. An audit is an impartial and objective appraisal or verification of the data, the procedures, or the performance of diverse operations, systems, activities, programs, functions, or funds, and of internal program and management controls. Audits are performed using professionally qualified auditors who meet and follow GAGAS. Such standards are issued by the Comptroller General of the United States and are to be followed by auditors and audit organizations. An internal audit is an audit performed by

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auditors employed by the audited organization. When audits are performed in accordance with GAGAS they provide reports that enhance the credibility and reliability of the information that is reported by and obtained from the organization being audited. Audits are performed to determine whether (1) government resources are managed properly and used in compliance with laws and regulations, (2) government programs are achieving their objectives and desired outcomes, and (3) government services are being provided efficiently, economically, and effectively.

Audits:

- Evaluate the integrity and reliability of financial and other management information used to make decisions;
- Determine whether laws, regulations, acceptable policies, and acceptable procedures are followed;
- Determine whether established standards and performance objectives are met;
- Determine whether resources are safeguarded and used efficiently and effectively; and
- Determine whether the desired results of an organization or program are being achieved.

Audits help management identify risks and arrive at solutions to problems, devise better ways of doing business, and deter fraud, waste, and abuse.

a. Types of Audit. There are three basic types of audit: financial audits, performance audits, and attestation engagements. Reference (b) provides detailed descriptions of these audits.

b. Staff Function. Internal audit is a staff function which, to be effective, must be independent of line operations. DON auditors do not exercise command authority over organizations they audit. Likewise, line organizations do not exercise command authority over the internal audit function. DON auditors impartially report the facts and, as appropriate, make recommendations to the level of management responsible for taking corrective action on conditions and opportunities for improvement disclosed by an audit. To do so, auditors must be free of personal impairments to independence that could affect their impartiality or the appearance of impartiality.

c. Part of Internal Control System. Internal audit is an integral part of the overall DON internal control and governance system designed to provide checks and balances to ensure

managers carry out their missions effectively and efficiently, and meet established goals and objectives. Reference (f) establishes the DON Management Control Program and requires commands to maintain effective systems of management control. Normally, internal auditors evaluate and report on management controls during every audit. Also, reference (f) requires that auditors evaluate and report on how well management has implemented the Management Control Program.

d. Local Audit Function. DON commands and activities may establish local audit functions to give local commanders an internal audit capability that complements the audits of the Naval Audit Service. DON local audit functions will report to the Head or Deputy Head, and will be organizationally located outside the staff or program management function, of the organization subject to audit. The local audit staff will not be used to perform operating tasks, but may be used for audit liaison and audit follow-up on internal audits done by others. Local audit staff may also be used to help commanders evaluate the adequacy of vulnerability assessments and perform or evaluate internal control reviews. See reference (g).

e. Separate from Inspection Function. The Naval Audit Service does not do inspections or inquiries, which are distinct from auditing in the nature of work done. DON organizations are authorized to request assistance from the Naval Audit Service when the nature of the assistance requires the expertise of auditors. The Naval Audit Service will honor those requests it determines reasonable and necessary.

6. Auditor General of the Navy and Naval Audit Service. Within DON, the Under Secretary of the Navy oversees internal audits (through the Office of the Auditor General) and resolves disputed audit findings. The Auditor General of the Navy is the senior DON advisor and assistant to the Secretary and Under Secretary of the Navy on all audit-related matters, per reference (e). The Auditor General establishes policy and procedures for internal auditing throughout the DON, and oversees all internal audits performed within the DON. The Auditor General of the Navy has overall responsibility over the Naval Audit Service. The Auditor General coordinates audits and maintains dialogue about audit matters with GAO, DoDIG, the Army Audit Agency, and the Air Force Audit Agency. The Naval Audit Service, as DON's internal audit agency, helps DON assess risk and audits DON organizations, programs, activities, systems, functions, and funds. No other office or entity in the DON

Secretariat, the Chief of Naval Operations Headquarters, or the Commandant of the Marine Corps Headquarters may set policy for or oversee DON's internal audits. The Naval Audit Service also:

a. Provides audit policy guidance for, and surveillance and review of, audits conducted by nonappropriated fund organization auditors and DON local audit organizations (reference (c));

b. Monitors DON contracts for audit services to ensure compliance with GAO and DoD audit guidance (reference (a));

c. Participates in the audit resolution process;

d. Supports the Naval Inspector General in executing the DON Audit Follow-up Program by keeping a data base showing the current status of management's actions in response to the findings, recommendations, and estimates of monetary benefits in Naval Audit Service audit reports and verifying corrective actions when and if a later audit is done (reference (h));

e. Serves as the focal point for internal audit policy for the DON Management Control Program (reference (f));

7. Policy

a. Independence and Impartiality of the Audit Function

(1) To ensure the independence and impartiality of the audit function, the Auditor General of the Navy reports directly to the Under Secretary of the Navy. Whenever the position of Under Secretary is vacant, the Auditor General of the Navy reports directly to the Secretary of the Navy. Within DON, only the Secretary of the Navy and the Under Secretary of the Navy may provide direction to the Naval Audit Service.

(2) Based primarily on a risk assessment developed in collaboration with DON senior leaders, the Auditor General will develop an annual plan of audits. Most audits in the annual plan will be developed using this collaborative risk-based process. However, the Auditor General also has the authority, in instances where he or she considers it appropriate, to independently decide the nature and scope of audits to be performed and the content of all audit reports.

(3) To comply with mandatory GAGAS, and ensure credibility of audit work, the Auditor General must ensure that:

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- In all matters relating to the audit work, the audit organization and the individual auditor are free, both in fact and appearance, from personal, external, and organizational impairments to independence;
- Professional judgment is used in planning and performing audits and in reporting the results; and
- The staff assigned to perform each audit collectively possesses adequate professional competence for the tasks required.

b. Audit Policy. The Inspector General, Department of Defense (DoDIG) establishes policy for auditing within DoD, including internal auditing, in compliance with GAGAS. The Auditor General of the Navy develops and implements DON audit standards, policies, and procedures consistent with GAO (reference (b)) and DoDIG guidance (references (a), (c), and (d)). See reference (e). When applied, these standards, policies, and procedures should offer adequate audit coverage of all DON organizations, programs, activities, and functions, including Marine Corps and nonappropriated fund organizations and related activities.

c. Audit Supervision

(1) The Auditor General of the Navy oversees the actual conduct of internal audits in DON by the Naval Audit Service; and oversees audits done by DON nonappropriated fund audit organizations (reference (c)), DON local audit functions, and nonfederal auditors (reference (a)) under DON contracts.

(2) Military officers may be assigned to the Naval Audit Service but may not supervise the conduct of audits. A military officer functioning as an auditor must be directly supervised by a qualified civilian auditor to ensure that recognized audit standards are followed. As with the civilian workforce, when a military officer's next assignment beyond the Naval Audit Service is known, he or she will not take part in an audit of that command or function.

d. Audit Funding. Per reference (c), the Naval Audit Service may request reimbursement for auditing nonappropriated fund organizations and related activities from the audited organization. All audit assistance in DON for appropriated fund and related activities will be done on a nonreimbursable basis. Audits of state government, local government, and non-profit organizations will be funded per reference (i). Peer Reviews

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conducted by the Naval Audit Service will be performed at no cost to the reviewed activity.

e. Operational Control. The Auditor General of the Navy has operational control over internal audits and other mission functions of the Naval Audit Service.

f. Audit Coordination. The Auditor General of the Navy will coordinate and cooperate with:

- the Naval Inspector General;
- the Director, Naval Criminal Investigative Service (NCIS);
- the DoDIG;
- other DoD audit services, including the Army Audit Agency and the Air Force Audit Agency; and
- GAO

to detect, deter, and document the occurrence and extent of fraud, waste, and related improprieties, and to avoid to the maximum extent possible duplicative effort (references (d), (e), (j), and (k)).

g. Command Support for Audit. The Secretariat and all DON echelons of command, including nonappropriated fund organizations and related activities, will provide, as required, suitable office space and all needed facilities in support of the audit function on a nonreimbursable basis.

8. Audit Planning. Early each fiscal year, the Naval Audit Service begins developing the following fiscal year's audit plan. The Auditor General of the Navy reviews the plan with the Under Secretary of the Navy before it is finalized.

a. Audit Research and Risk Assessment. First, a risk assessment will be developed in collaboration with DON senior leaders. At the same time, auditors research and review programs, functions, and risk areas having potential for audit. Echelon I and II DON management officials are asked to provide input to the risk assessment, and to submit audit topic suggestions. After the risk assessment and Naval Audit Service research are completed, resulting topics and all other categories of audit are developed and ranked, and a draft annual audit plan is developed.

b. Coordination with Other Offices. Local internal audit functions, local nonappropriated fund audit organizations, and military exchange audit organizations will provide their annual

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audit plans to the Naval Audit Service by 31 July. The Naval Audit Service will also take part in the DoDIG functional Joint Audit Planning Groups and coordinate with GAO, DoDIG, and other military service audit organizations in developing the audit plan. When beginning the execution of planned audits, Naval Audit Service will coordinate, as appropriate, with other applicable audit and inspection organizations.

9. Access to Information. Consistent with security requirements, DON auditors must be granted full and unrestricted access to all personnel, facilities, records, reports, data bases, documents, or other DON information or material that the Auditor General deems necessary to accomplish audit related matters. All DON personnel shall respond to any request or inquiry by the Auditor General of the Navy within the scope of the audit function, as if made by the Secretary of the Navy. All access granted, property or services provided, or information or material given to the audit organizations will be on a nonreimbursable basis. This includes automated data processing support, data retrieval, and programming, as needed, to do the audit.

a. Access to Personnel, Documents, and Records. Consistent with appropriate security clearances, auditors shall be granted full and unrestricted access to personnel, documents, and records. Such access will be unrestricted and unfettered by burdensome administrative requirements or screening procedures beyond those required by security regulations. Access to ships, squadrons, and fleet marine force units will follow the policy established in enclosure (1) of reference (1).

b. Access to Automated Data Processing Equipment. Access to automated data processing equipment (including microcomputers and on-line workstations), databases, and programming personnel must be readily made available to the Naval Audit Service auditors to allow auditing of automated information. Necessary access to, and related training on, existing data retrieval and report generating capabilities will also be provided to Naval Audit Service auditors.

c. Access to Privacy Act Data. Reference (m) implements provisions of the Privacy Act of 1974. Under the instruction, auditors have access to all records covered by the Act when discharging their official duties, e.g., when planning, researching, or auditing. Activities providing auditors such access are exempt from disclosure requirements.

d. Access to OGE Forms 450 and SFs 278. Naval Audit Service auditors will be given access to Executive Branch Confidential Financial Disclosure Reports (OGE Forms 450) and Executive Personnel Financial Disclosure Reports (SFs 278) if the auditors decide they are needed to perform audit functions, including audit planning, audit research, and audit execution.

e. Conditional Access - Source Selection Information. Before being given access to source selection information, auditors may be required to sign nondisclosure agreements if and only if program personnel are required to sign similar agreements at the time access is requested.

f. Access Denial. Only the Secretary of the Navy and the Under Secretary of the Navy may deny access to DON auditors. A disagreement between auditors and managers as to the need for access to information will be reported promptly through proper audit and command channels to the management level necessary to resolve the issue. Such denials will only be for reasons necessary to preserve the national security interests of the United States, as provided in section 8 of the Inspector General Act of 1978, reference (n). The Auditor General will inform the Under Secretary of the Navy of the denial of access immediately upon the determination that the issue cannot be resolved at a lower level. The Under Secretary will make a decision on the denial issue within 30 workdays of notification by the Auditor General of the denial. If the Under Secretary of the Navy considers it proper to deny access, the DoDIG must be told within 15 workdays of the denial decision (reference (a)).

10. Audit Execution

a. Notice. When possible, approximately 30 days before beginning a scheduled audit, the Naval Audit Service will send an announcement letter to the affected organizations and their superiors in the chain of command. The letter encourages recipients to suggest areas of particular concern for intensified audit coverage. Normal 30-day notification will not be given for:

- Scheduled audit research efforts, where verbal notice is generally given;
- Unscheduled audit work such as audit research where 30-day notification is impractical; and

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- Unannounced audits, where the notice is hand-delivered by auditors to the commander or senior official on the first day of the audit.

The absence of 30-day notification will not be used to deny or delay access to information needed to perform the audit function.

Disclosure of a material or sensitive issue during audit research may result in immediate reporting and converting of research effort into a formalized, limited-scope audit. The Naval Audit Service will tell audited commanders or senior officials of the circumstances requiring such a change. When such circumstances arise, commanders or senior officials should tell their immediate superior in the chain of command.

b. Repeat Findings. The Naval Audit Service will follow up on findings and recommendations from the most recent Naval Audit Service audits (and, when appropriate, from audits performed by GAO, DoDIG, or other audit organizations) of the organization, activity, program, or function under review, if such audits are no more than three years old. If stated corrective action was not taken or was not effective in correcting the reported condition, a repeat finding will be included in the current audit report. Repeat findings are addressed to the immediate superior in the chain of command above the earlier action addressee.

c. Draft Findings. During the field work phase of an audit, findings are developed and discussed with cognizant operating personnel, division managers, and department heads. These discussions verify supporting facts and obtain preliminary feedback on conclusions reached. They also enhance management's ability to correct problems early.

d. Audit Utilization. The audit utilization process is the continuous communication between auditors and managers during an audit in an effort to inform management of audit findings and recommendations, ensure the accuracy of facts presented, and provide management the opportunity to put audit results to use as soon as they become known. To maximize the benefits of an audit, auditors and DON managers must gain a common understanding of problems disclosed by the audit, of potential solutions to correct those problems, and of the potential monetary benefits to be gained through improved management actions, if any. Audit utilization is the formal process which

serves to achieve these ends. Auditors issue a draft report for comment to the action addressee (i.e., the lowest level manager at the audited program, function, or activity who can take the corrective action recommended in the audit report). Copies of the draft report are also sent to one level of management above the addressee and to the manager requesting the audit. The draft report is provided to ensure that audit results are accurately, fairly, and impartially presented and to reach agreement with management on specific and realistic audit recommendations, completion dates for implementing the recommendations, potential monetary benefits, and material internal control weaknesses. Utilization above the Secretary of the Navy, Chief of Naval Operations, and Commandant of the Marine Corps levels requires approval of the Auditor General of the Navy or his or her designee. Note, findings will be discussed with various key DON officials as the audit progresses.

e. Releasability of Draft Findings and Draft Reports. Draft audit findings and reports are predecisional material internal to the DON and, as such, are not releasable outside the DON except by specific approval of the Auditor General of the Navy. When draft reports are sent to the action addressees, the addressee will be asked to identify, and give an explanation for, any parts of the draft report that they believe should not be released to the public under the Freedom of Information Act (FOIA) in the final audit report. Final reports may be published with undecided recommendations. Final reports are not considered predecisional and are subject to release under FOIA.

f. Monetary Benefits. Monetary benefits associated with audit findings arise from actions such as collecting money erroneously paid out, identifying excess material, deobligating funds (current or expired), avoiding unnecessary expenditures, increasing productivity, and improving procedures to enable an organization to do a function more efficiently. Identification of potential monetary benefits can provide a perspective in judging the importance and materiality of the condition and the recommended corrective actions. Monetary benefits are classified as either funds available for other use or questioned costs under the Inspector General Act of 1978, reference (n). Amounts claimed are normally limited to a six-year period covered by the Future Years Defense Plan (FYDP) or the Program Objectives Memorandum (POM).

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(1) Potential monetary benefits will be discussed in audit reports but amounts will not be included in specific audit recommendations. This policy allows the auditor and the manager to concentrate on a remedy without unduly focusing on the potential effects of the efficiencies to be gained by applying the recommendations. Management's written position on an audit recommendation must include a separate comment on potential monetary benefits indicating concurrence or nonconcurrence with the specific amount of claimed benefits, or offering a recomputation of the probable benefit to help track such efficiencies in the DON formal follow-up system. A failure to address potential monetary benefits in the management response to an audit report results in those potential benefits, and associated recommendation(s), being reported as undecided and subject to the formal audit resolution process.

(2) Potential monetary benefits may be authoritatively claimed based on statistical sampling.

g. Management Responses to Findings. Recommendation addressees are given a reasonable period of time to respond in writing to Naval Audit Service findings, generally 30 calendar days. Reasonable extensions may be granted; but extensions must be fully justified and are not granted routinely. Management responses not received in the allowed timeframe may result in the audit report being published without a management position. In such cases, recommendations will be considered undecided and subject to the audit resolution process, which process is facilitated by the Naval Inspector General.

(1) Responses should express explicit concurrence or nonconcurrence with all elements of a finding (on the facts, conclusions, recommendations, and if applicable, potential monetary benefits) in clear and simple language with emphasis on improvement. Management comments should address unusual circumstances which may have contributed to an operating deficiency and describe the corrective actions taken or planned. If management has a preferred alternative for correcting the problem, it should be clearly explained in the response statement. Concurrence with a finding and recommendation must be accompanied by completion dates for actions taken, the estimated potential benefits, and realistic and reasonable target dates for carrying out planned corrective actions. When corrective actions are to be taken over an extended period (in excess of one year), management must establish interim dates for

completing major segments of the planned corrective actions. This policy follows reference (h).

(2) The Naval Audit Service evaluates management responses to reports and may change or drop findings, recommendations, or potential monetary benefits based on such evaluations. Significant changes to findings are discussed with the proper addressee(s) before the final audit report is published. Management comments received before report publication will normally be included verbatim in the final audit report.

(3) If the management position specifies concurrence with the facts and recommendations in a finding, but does not agree with the audit's suggested potential monetary benefits, the management position on the reported monetary benefits and the associated recommendations will be treated as an undecided issue. Also, if management does not state a specific position on the potential monetary benefits, the monetary benefits and the associated recommendation(s) will be treated as an undecided issue.

(4) DON policy considers nonreceipt of a management response as nonconcurrence. The Auditor General of the Navy will promptly bring nonreceipt of a response to a recommendation or untimely response issues to a higher level of DON management for action. The Auditor General of the Navy will elevate a nonconcurrence to a finding, recommendation, or potential monetary benefit in a published report to a higher level of DON management for a decision, including directly to the Under Secretary of the Navy when considered appropriate.

(5) Undecided issues in an audit report will not prevent or unduly delay the report's publication.

(6) By statute, reference (o), all undecided audit findings must be decided within six months of the date of the final audit report. The Under Secretary of the Navy is the DON's final authority for adjudicating internal audit findings, recommendations, and potential monetary benefits when management and the auditors cannot reach agreement.

11. Distributing Final Reports

- a. Within DoD. Final written reports are to be sent to:

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- (1) The commanding officer or program manager of the program, function, or activity audited;
- (2) Officials who requested the audit;
- (3) All officials responsible for corrective actions;
- (4) Key stakeholders;
- (5) Naval Inspector General for audit follow-up; and
- (6) All others who request and are authorized to receive such reports.

Unless restricted by law or Office of Management and Budget (OMB), DoD, or DON guidance, copies should be made available for public inspection under FOIA procedures. Related audit working papers, documents, and files will be kept for a minimum of three years after issuing the final audit report or two years after all recommendations are closed, whichever is longer. Upon request, final reports will be made available to the Office of the DoDIG.

b. GAO, Congress, and the Courts. The Auditor General may release to the following Government officials published audit reports, outside FOIA and at no cost to the requestor, if the officials are requesting the reports in their official capacity on behalf of the Governmental body:

- (1) A GAO auditor;
- (2) A member of Congress, a Committee or Subcommittee of Congress, or either House sitting as a whole; or
- (3) A Federal court, whenever ordered by officers of the court as necessary for properly administering justice.

Note, even though authority may exist to show records to such individuals in their official capacity, FOIA applies if the same individual seeks the records in a private or personal capacity. Thus, a request from a member of Congress made on behalf of his or her constituents must be processed under FOIA.

To adequately protect documents given to Government officials, the Auditor General will tell officials that the documents are, and will mark the records as, "Privileged" and "Exempt from Public Disclosure" and annotate any special handling instructions on the report as required by reference (p). Classified information remains subject to reference (q) and Privacy Act information remains subject to reference (m).

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c. FOIA Requests. The Auditor General of the Navy is the initial release and denial authority for all Naval Audit Service audit reports. See references (p) and (r). All requests for draft and final Naval Audit Service audit reports and other Naval Audit Service records should be promptly sent to Naval Audit Service. Reference (m) states that a DON activity receiving such a request will inform the requestor of the correct procedure.

The cognizant commanding officer for local audit and nonappropriated fund audit reports responds to such requests. The responsible official for responding to such requests for nonappropriated fund audit reports in the Marine Corps is the Headquarters, U.S. Marine Corps FOIA Manager.

Affected activities will be given an opportunity to comment on public disclosure of any undecided findings or recommendations. After considering such comments, the Auditor General will determine if any undecided findings or recommendations should be withheld until resolution or six months after the report is published, whichever occurs first. Arguments that the findings or recommendations should be withheld simply because management and the Naval Audit Service disagree, or because disclosure would embarrass the DON, are not considered sufficient reasons to withhold an undecided finding or recommendation under FOIA. When a final report having undecided issues is disclosed under FOIA, the Auditor General will tell the FOIA requester that the final report has such undecided issues.

12. Audit Resolution. The Under Secretary of the Navy is the Resolution Authority for unresolved audit findings, recommendations, and monetary benefits. By statute, reference (o), all unresolved audit findings and recommendations must be resolved within six months of the date of the final audit report. DON policy in reference (h) requires prompt, responsive, and constructive actions by commanding officers on audit recommendations. The Naval Audit Service will address repeat findings to the immediate superior in command above the auditee level for resolution.

13. Follow-Up of DON Internal Audits

a. Definition. Audit Follow-up is the collective effort to ensure that management takes prompt, effective, and coordinated

corrective action to implement audit report recommendations and that controls are adequate to prevent the recurrence of identified weaknesses. It includes monitoring, reporting on, and validating management's actions in response to the recommendations of published audit reports. Audit follow-up is an integral part of good management and is a responsibility shared by DON managers and auditors.

In the DON audit follow-up process, the following definitions apply:

(1) *Open*. Action on a concurred-in or decided recommendation has or will be completed after the audit report is published or when management agrees that a potential monetary benefit exists, but an agreed-upon amount requires more time to compute.

(2) *Closed*. Necessary management action on findings, recommendations, and claimed funds available for other use is decided or agreed upon, and corrective action has been completed and documented.

(3) *Decided*. An agreement has been reached between management and auditors on previously undecided findings, recommendations, questioned costs, and funds available for other use or a decision has been made by the Resolution Authority settling the disagreement. A recommendation decided in favor of the audit position may be open or closed depending on the status of corrective actions taken.

(4) *Undecided*. No agreement has been reached between management and auditors on a finding, recommendation, questioned cost, or potential funds available for other use.

b. Accountability. The Naval Inspector General is accountable to the Under Secretary of the Navy for the DON Audit Follow-Up function per references (h) and (e). The Naval Inspector General has issued procedures for DON audit follow-up in reference (h).

c. Monitoring. The Naval Audit Service will keep a data base capable of tracking the status of all findings and recommendations, including associated potential monetary benefits, i.e., potential funds available for other use and questioned costs, for Naval Audit Service audit reports from the time audit reports are issued through implementation of

corrective actions. Commanding officers of local audit functions will ensure the maintenance of similar data bases capable of tracking the status of all findings and recommendations for their audit reports.

Navy activities and the Commandant of the Marine Corps will provide the basic follow-up information for the Naval Audit Service database to the Naval Audit Service. This input should be provided within 30 days after either the final report publication date, or the actions or determinations described below, whichever is later. The required input data are:

(1) Estimated completion date of previously agreed to but not yet completed actions.

(2) Revised target date when the original target date given during the audit utilization process cannot be met.

(3) Changes to previously agreed to actions with enough detail to enable the Auditor General of the Navy to decide if the finding can be closed.

(4) Reversal of earlier agreements to take recommended actions.

(5) Final determination of recommendations or associated potential monetary benefits, i.e., specific amounts available for other use and questioned costs previously undetermined in the utilization process.

(6) Resolution of previously undecided findings, recommendations, or associated potential monetary benefits, i.e., potential funds available for other use and questioned costs.

The Naval Audit Service does selective follow-up audits and on-site verification reviews if, within three years, it does an audit in the same area. Such reviews evaluate the follow-up process and the actions taken by management to correct significant deficiencies involving material management control weaknesses, repeat findings, or funds available for other use.

d. Reporting. The Naval Inspector General monitors and reports on audit follow-up per reference (h).

14. Fraud, Waste, and Related Improprieties

a. General. Deterring and preventing fraud, waste, and related improprieties are among the prime responsibilities of management. The principal mechanism for preventing and detecting fraud and illegal acts is an effective management control system.

b. Internal Auditors. Internal auditors are instrumental in ensuring controls are in place to prevent fraud, waste, and related improprieties. Audits may also detect vulnerabilities to fraud, waste, and abuse. GAGAS (reference (b)) require auditors to be alert to situations or transactions that could indicate fraud, waste, and abuse.

(1) GAGAS states that, where an auditor's work includes an assessment of compliance with laws and regulations, the work should be designed to provide reasonable assurance of detecting fraud or illegal acts that could significantly affect the audit objectives.

(2) All DON auditors must ensure that copies of all procurement-related fraud reports are given to the Director, Acquisition Integrity Office (AIO), who will coordinate appropriate remedial actions per reference (j). Also, all DON auditors must ensure that NCIS is informed of actual or suspected criminal activities (reference (j)).

c. Suspected Fraud Reports. When DON auditors suspect criminal activity, they will report the suspected fraud to NCIS and, if acquisition-related, NCIS will report it to the AIO. When criminal activity is suspected during the audit, any related audit findings will not refer to criminal statutes, to the possible occurrence of a crime, or to the existence of criminal intent. Related audit findings will only address non-criminal aspects of fraud or other criminal activities, such as mismanagement and improper practices. Any notification or dissemination of audit reports will be coordinated with NCIS to prevent compromise of the investigation, or destruction or alteration of evidence.

d. Criminal Investigations. Auditors do not conduct criminal investigations. That is the responsibility of investigators or law enforcement authorities. However, auditors are responsible for notifying NCIS when they identify indicators of fraud. Also, the Naval Audit Service will provide audit support, when appropriate and requested by NCIS.

15. Use of Investigators on Audits. The Naval Audit Service coordinates and cooperates with NCIS to ensure effective oversight coverage of DON programs and operations.

a. Whenever NCIS investigators are part of an audit team, they will be under the direction of the supervisory auditor. The command will be told of the investigators' presence only with the concurrence of the Director, NCIS.

b. The Naval Audit Service does not perform an investigative function. The Naval Audit Service only identifies the possibility of fraud.

c. Assistance to investigators will be given as approved by the Auditor General of the Navy.

16. Contracting for Audit Services. Before a DON command or activity contracts for audit services, the DON command or activity must inform, and obtain approval from, the Auditor General of the Navy. See paragraph b below. No DON command or activity will contract for audit services unless the expertise required to do the audit is not available within DON or temporary audit help is needed to meet audit reporting requirements mandated by law or regulation. The only exceptions to this policy are audits of nonappropriated fund organizations and related activities as authorized by reference (c). Also, no DON command or activity will contract for a quality assurance review of internal audit or local audit without going through the proper chain of command and obtaining the prior approval of the DoDIG (reference (a)).

a. Naval Audit Service Responsibilities. The Auditor General of the Navy will provide oversight to ensure that contracted audits meet audit objectives and GAGAS. The Naval Audit Service will:

(1) Review proposed contract statements of work, special provisions, general provisions, and data requirements before solicitation;

(2) Periodically monitor the progress of the nonfederal auditors under contract to do audits;

(3) Give, when requested, technical guidance to nonfederal auditors under the contract; and

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(4) Do pre-acceptance reviews of completed work under awarded contracts before final contract payment.

b. Command Responsibilities. DON commands and non-appropriated fund activities will ensure that:

(1) Proposed contracts that include audit services within the statement of work are coordinated with and approved by the Auditor General of the Navy before a solicitation package (or if no solicitation package, before a contract) is issued. The completed solicitation package (or proposed contract), including the statement of work, the general provisions, the contract data requirements, and any proposed special provisions, will be provided to the Auditor General for this approval process.

(2) All audit proposals from nonfederal auditors include the dates and results of the latest peer review made of their firm, if any. Commands and activities should not contract for audit services with any firm that has not successfully passed a peer review within the preceding three years as required by GAGAS.

(3) Proper security clearances are obtained for nonfederal auditors.

(4) Copies of contracts awarded, including all modifications, that include audit services are sent to the Auditor General of the Navy upon execution.

(5) Copies of audit reports and, if requested, working papers obtained under contracts are sent to the Auditor General of the Navy for review and comment before final contract payment.

(6) Recommendations originating from audit work done under contract are decided at proper management levels and followed up on per reference (h).

c. Contract Provisions. All contracts that include audit services involving nonfederal auditors, including contract renewals, must include specific provisions requiring the contractors to:

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(1) Allow Government technical representatives and DON auditors to review and make copies of work papers, including audit plans and programs, and draft reports prepared during contract performance.

(2) Preserve the work papers, records, and other evidence of audit for at least three years following the report date. During this time, the nonfederal auditors will make the audit material available to the command, to the Naval Audit Service, and to the Office of the DoDIG upon request.

(3) Follow GAGAS (references (a), (b), and (d)) in auditing.

(4) Give an opinion on the adequacy and effectiveness of the internal controls within the scope of their engagement. This opinion will be based on the results of the survey phase or the audit verification phase evaluation of management controls and on compliance with DON instructions in those areas covered by the contracted audit.

(5) Rely on the work of Federal auditors, providing that such auditors and their work meet GAGAS (references (a), (b), and (d)).

(6) Explain to government personnel their audit procedures, working papers, and findings related to the contract effort until all audit findings and disputes are decided.

(7) Provide a written evaluation of the audit comments submitted by the audited activity in response to the audit report's findings, recommendations, and potential monetary benefits.

(8) Refer instances of suspected fraud through the Naval Audit Service to NCIS. Prior coordination with Naval Audit Service is necessary.

(9) Give a copy of all audit-related contract deliverables, including the final audit report, to the Auditor General of the Navy.

17. Quality Control and Assurance

a. Professional Qualifications and Training. All auditors responsible for planning, directing, conducting, or reporting on

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government audits will complete, every two years, at least 80 hours of continuing education and training that contributes to the auditor's professional skill. At least 20 hours should be completed in any one year of the two-year period. Individuals responsible for planning, directing, or conducting large parts of the field work or reporting on the Government audit will complete at least 24 of the 80 hours of continuing education and training in subjects directly related to the Government environment and to Government auditing.

b. Internal Quality Assurance. Each DON audit organization will establish and maintain an appropriate internal quality control system that will give reasonable assurance that the audit organization has implemented and fully complied with applicable auditing standards, policies, and procedures. See chapter 7 of the DoDIG Internal Audit Manual, reference (d).

c. External Quality Assurance Reviews. Each DON audit organization will take part in an external quality assurance review at least once every three years. The Naval Audit Service will do the external quality assurance review of DON local audit and nonappropriated fund audit organizations. The external quality assurance review program will determine whether the audit organization's internal quality control system is in place and operating effectively and whether established policies and procedures and applicable audit standards are being followed in its audit work. See chapter 7 of the DoDIG Internal Audit Manual, reference (d).

18. Administration and Maintenance. Recommendations for improvements and changes to this instruction, with justification, should be sent to the Auditor General of the Navy.



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Under Secretary of the Navy

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